Supreme Court, U.S.
FILED
JAN 8 1990
JOSEPH F. SPANIOL, JR.
CLERK

NO. 89-935

IN THE

Supreme Court of the United States

OCTOBER TERM, 1989

LIVELY EXPLORATION COMPANY, ET AL.,
Appellants

VS.

VALERO TRANSMISSION COMPANY,
Appellee

FROM NO. 04-87-00380-CV
IN THE COURT OF APPEALS FOR THE
FOURTH SUPREME JUDICIAL DISTRICT OF TEXAS
AT SAN ANTONIO, BEXAR COUNTY, TEXAS

MOTION TO DISMISS APPEAL AND, ALTERNATIVELY, TO AFFIRM JUDGMENT

J. CLIFFORD GUNTER III

BRACEWELL & PATTERSON
2900 South Tower Pennzoil Place
Houston, Texas 77002
(713) 223-2900

Counsel for Appellee

January 6, 1990

Alpha Law Brief Co., Inc. — 8748 Westpark — Houston, Texas 77063 — 789-2000

TABLE OF CONTENTS

		Page
Table of Contents		i
Table of Authorities		ii, iii
List of Companies Affiliated With Valero Transmission Company		iv
I.	*Overview*	2
II.	*This Appeal is Not Within this Court's Jurisdiction and Cannot be Taken in Accordance with Statute*	2
III.	*Statement of the Case Relevant to Other Grounds for Dismissal*	6
	A. *The Parties.*	6
	B. *The Contract.*	7
	C. *Relevant Laws and Regulations.*	9
	D. *The Interface Between the Gas Market Demand Rule and the Contract.*	11
	E. *Lively's Lawsuit and Appeal.*	12
IV.	*Lively Failed to Timely Raise the Points of Error Upon Which it Appeals to This Court*	15
V.	*Lively Raises No Federal Question at All, Much Less a Substantial One*	20
VI.	*The Judgment of the Court Below Should be Affirmed*	24
VII.	*Conclusion and Prayer*	24

TABLE OF AUTHORITIES

CASES

	Page
American Ry. Exp. v. Levee, 263 U.S. 19, 20-21 (1923) ...	4
Andrews v. Virginian Ry., 248 U.S. 272, 274-75 (1919) ...	3-6
ANR Pipeline Co. v. Corporation Comm'n of the State of Okla., 860 F.2d 1571 (10th Cir. 1989), *cert. denied*, _____ U.S._____, 109 S. Ct. 1967, 104 L.Ed.2d 435 (1989) ...	22
Banks v. California, 395 U.S. 708 (1969)	3
Brinkerhoff-Faris Trust & Savings Co. v. Hill, 281 U.S. 673 (1930)	19
Chicago Great W. R.R. v. Basham, 249 U.S. 164, 167 (1919)	3, 4
Clark v. Jeter, 486 U.S. 456, 108 S. Ct. 1910 (1988)	19, 20
Costarelli v. Massachusetts, 421 U.S. 193, 196 (1975)	6
Exxon Corp. v. Eagerton, 462 U.S. 176, 185-87 (1983) ..	23
Frio Investments, Inc. v. 4IMC/Rohde, 705 S.W.2d 784, 787 (Tex. App.—San Antonio 1986, writ ref'd n.r.e.) ..	18
Gillen v. Diadrill, Inc., 624 S.W.2d 259, 264 (Tex. App.—Corpus Christi 1981, writ dism'd)	16
Great N. Ry. Co. v. Sunburst Oil & Refining Co., 287 U.S. 358 (1932)	19
Herndon v. State of Ga., 295 U.S. 441 (1935)	18
Lone Star Gas Co. v. Sheaner, 305 S.W.2d 150, 153 (Tex. 1957)	16
Market St. Ry. v. Railroad Comm'n, 324 U.S. 548, 551 (1945)	3
Michigan-Wisconsin Pipeline Company v. Calvert, 347 U.S. 157, 159 (1954)	3
Norton v. Martin, 703 S.W.2d 267, 273 (Tex. App.—San Antonio 1986, writ ref'd n.r.e.)	18
Northern Natural Gas Co. v. State Corp. Comm'n of Kan., 372 U.S. 84 (1962)	21, 22
Northwest Central Pipeline Corp. v. State Corporation Comm'n of Kan., _____U.S._____, 109 S. Ct. 1262, 1274-75, L.Ed.2d 509 (1989)	23
Pike v. Bruce Church, Inc., 397 U.S. 137 (1970)	23
Samples Exterminators v. Samples, 640 S.W.2d 873, 875 (Tex. 1982)	18
Sandquist v. California, 419 U.S. 1066 (1974)	3
State of Mo. v. Gehner, 281 U.S. 313 (1930)	19
Stratton v. Stratton, 239 U.S. 55, 56-57 (1915)	3
Transcontinental Gas Pipeline Corp. v. State Oil & Gas Bd. of Miss., 474 U.S. 409 (1986)	21-23
United States v. Walter, 44 S. Ct. 10, 12 (1923)	4
Watson v. Glens Falls Ins. Co., 505 S.W.2d 793, 797-98 (Tex. 1974)	16

STATUTES

	Page
16 Tex. Admin. Code § 3.30	10
16 Tex. Admin. Code § 3.34	10
16 Tex. Admin. Code § 3.91	10
28 U.S.C. § 1257 (West. Supp. 1989)	2, 3, 6
H.R. Rep. No. 660, 100th Congress, 2nd. Sess. 12, *reprinted in* 1988 U.S. Code Cong. & Admin. News 766, 779	6
Sup. Ct. R. 12, 28 U.S.C.A. 18 (1984)	4
Sup. Ct. R. 16(b), 28 U.S.C.A. 30-31 (1984)	15, 20
Tex. Nat. Res. Code Ann. § 85.051 (1978)	10
Tex. Nat. Res. Code Ann. § 85.052 (1978)	10
Tex. Nat. Res. Code Ann. § 86.001, et seq. (1978)	10
Tex. Nat. Res. Code Ann. § 86.011 (1978)	10
Tex. Nat. Res. Code Ann. § 86.012 (Supp. 1989)	10
Tex. Nat. Res. Code Ann. § 111.081, et seq. (1978 & Supp. 1989)	10
Tex. Nat. Res. Code Ann. § 111.083 (1978)	10
Tex. Nat. Res. Code Ann. § 111.086 (1978)	10
Tex. R. App. P. 52(a)	16
Tex. R. Civ. P. 74(d)	16
Tex. Rev. Civ. Stat. arts. 6050-53 (Vernon 1962 and Vernon Supp. 1987)	9

LIST OF COMPANIES AFFILIATED WITH VALERO TRANSMISSION COMPANY

Valero Transmission Company, formerly a corporation, has become a limited partnership, Valero Transmission, L.P. During the time it was a corporation, its parent corporation was Valero Energy Corporation. It had no subsidiary corporations. Corporations in any way affiliated with it were: -

Valero Coal Company
Valero Management Company
Valero Land Company
Valero Natural Gas Company
Valero Communications Company
Valero Realty Company
Valero Refining and Marketing Company
J & R Coal Company
ESCO Supply Company
Valero Building Company
Rio Grande Valley Gas Company
Valero Refining Company
Valero Petroleum Marketing Company
VMGA Company
Valero Interstate Transmission Company
Valero Investor Services, Inc.
Valero Eastex Pipeline Company
R.G.V. Consumer Service Company
Corpus Christi Marine Services Company
Valero Oil International, Ltd.
Rio Pipeline Company
Valero Storage Company
Valero Gas Storage Company
VLDC Company
Val Gas Company
V.H.C. Gas Systems Company
Mesquite Services Company
Valero Industrial Gas Company
Valero Hydrocarbons Company
Valero Marketing Company
V.H.C. Pipeline Company
Valero Gathering Company
Reata Industrial Gas Company

NO. 89-935

IN THE

Supreme Court of the United States

OCTOBER TERM, 1989

LIVELY EXPLORATION COMPANY, ET AL.,
Appellants

VS.

VALERO TRANSMISSION COMPANY,
Appellee

FROM NO. 04-87-00380-CV
IN THE COURT OF APPEALS FOR THE
FOURTH SUPREME JUDICIAL DISTRICT OF TEXAS
AT SAN ANTONIO, BEXAR COUNTY, TEXAS

MOTION TO DISMISS APPEAL AND, ALTERNATIVELY, TO AFFIRM JUDGMENT

To The Honorable United States Supreme Court:

Valero Transmission Company ("Valero"), appellee, files this Motion to Dismiss Appeal, and, Alternatively, to Affirm Judgment.

I. Overview

This case involves the state law question of whether Valero, an intrastate pipeline, breached a gas purchase contract with appellants Lively Exploration Company, et al. ("Lively"). Valero seeks dismissal of Lively's appeal for the following reasons: (i) the appeal cannot be taken in conformity with the amended 28 U.S.C. § 1257 (West Supp. 1989); (ii) the appeal is not within this Court's jurisdiction; (iii) the alleged "federal questions" were neither timely and properly raised nor expressly passed on; (iv) no federal question at all is presented, much less a substantial one; and (v) the court of appeals judgment rests on an adequate non-federal basis. Alternatively, Valero seeks affirmance of the court of appeals judgment.

II. This Appeal is Not Within this Court's Jurisdiction and Cannot be Taken in Accordance with Statute

This Court has no jurisdiction to consider this appeal, and it cannot be taken in accordance with 28 U.S.C. § 1257 (West Supp. 1989) ("§ 1257").

After the trial court entered judgment in this case against Lively, Lively appealed. On March 31, 1988, the court of appeals affirmed the trial court's judgment. (Lively's Appendix, pp. 36-37). Lively applied for a writ of error to the supreme court of Texas, which denied its application on June 7, 1989, and denied Lively's motion for rehearing on September 13, 1989. (Lively's Appendix, pp. 32-35).

Effective September 25, 1988, § 1257 was amended to eliminate an appeal for final judgments entered on

or after that date. The court of appeals judgment did not become final for jurisdiction purposes until the Texas supreme court denied rehearing on September 13, 1989. *Market St. Ry. v. Railroad Comm'n*, 324 U.S. 548, 551 (1945); *Chicago Great W. R.R. v. Basham*, 249 U.S. 164, 167 (1919); *Andrews v. Virginian Ry.*, 248 U.S. 272, 274-75 (1919). Therefore, Lively's appeal is foreclosed.

It is true that where the Texas supreme court has refused an application for writ of error, an appeal to the United States Supreme Court is properly from the court of civil appeals. *Michigan-Wisconsin Pipeline Co. v. Calvert*, 347 U.S. 157, 159 (1954). However, the date of the court of appeals judgment does not determine whether the amendment to § 1257 applies.

Review of a court of appeals judgment by the state supreme court must be sought before this Court has jurisdiction to review it. *Sandquist v. California*, 419 U.S. 1066 (1974); *Banks v. California*, 395 U.S. 708 (1969); *Stratton v. Stratton*, 239 U.S. 55, 56-57 (1915). To be "final" so as to give rise to this Court's jurisdiction, a judgment must be "subject to no further *review* or correction in *any other state tribunal*; . . . . [The judgment] must be the final word of a final court." *Market St. Ry.*, 324 U.S. at 551 (emphasis supplied). Until the Texas supreme court's denial of the motion for rehearing, the court of appeals judgment was "subject to . . . further review or correction [by another] state tribunal," *id.*, and therefore was not final for jurisdictional purposes.

Moreover, the time limit for applying to this Court for relief runs from the date the state supreme court refuses writ or rehearing, not from the date of the court

of appeals' decision. *United States v. Walter*, 44 S.Ct. 10, 12 (1923); *American Ry. Exp. v. Levee*, 263 U.S. 19, 20-21 (1923). Lively notes that it docketed its appeal "within 90 days from the denial of rehearing by the Texas Supreme Court" (Jurisdictional Statement, p. 3); this Court's then-applicable rules provided for docketing "90 days after the entry of the *judgment appealed from.*" Sup. Ct. R. 12, 28 U.S.C.A. 18 (1984). By necessarily equating the "denial of rehearing" with the "judgment appealed from," Lively illustrates that, for jurisdictional purposes, the court of appeals judgment cannot have been finally "entered" until denial of rehearing by the Texas supreme court.

Chicago Great W. R.R. and *Andrews* are closely on point. In *Chicago Great W. R.R.*, the Judicial Code then in effect, which governed review of state court decisions by this Court, had been amended to specifically delineate jurisdiction exercisable by writ of error as opposed to writ of certiorari. *Id.* at 165. The amendment provided that the right of review under existing laws with respect to judgments entered before the act took effect (October 6, 1916) should remain unaffected for the period of six months thereafter. *Id.* at 166. Within the six-month period, petitioner applied for a writ of error that did not come within this Court's jurisdiction under the Amendment. *Id.* at 165-66. Noting that whether its jurisdiction was properly raised "depends upon whether the judgment sought to be reviewed was 'entered before this act takes effect' within the meaning of [the amendment]," *id.*, this Court concluded the judgment could not be considered final until December 18, 1916, the date the state supreme court denied the second petition for rehearing:

> It is only a judgment marking the conclusion of the course of litigation in the courts of the state that is subject to our review. Hence, whatever its form of finality, if a judgment be in fact subject to reconsideration and review by the state court of last resort through the medium of a petition for rehearing, and such a petition is presented to and entertained and considered by that court, we must take it that by the practice prevailing in the state the litigation is not brought to a conclusion until this petition is disposed of, and until then the judgment previously rendered cannot be regarded as a final judgment within the meaning of the act of Congress.

Id. at 167. Therefore, the writ of error was dismissed. *Id.*

In *Andrews* this Court considered the same amendment and reached the same conclusion. Petitioner sought a writ of error to a trial court judgment that was rendered on June 16, 1916, but on which the court of appeals had denied writ of error on November 13, 1916. *Id.* at 273. Dismissing the subsequent writ of error for want of jurisdiction, this Court stated:

> Undoubtedly, before the action of the Court of Appeals, the judgment was not final and was susceptible of being reviewed and reversed by that court. Undoubtedly, also, until the Court of Appeals acted, the trial court was not the court of last resort of the state whose action could be here reviewed. The contention, therefore, that the judgment of the trial court was a final judgment susceptible of being here reviewed by writ of error must rest upon the impossible assumption that the finality of that judgment existed before the happening of the cause by which alone finality could be attributed to it.

Id. at 274. This Court noted that any other rule would render a judgment "open at the same time to the power of a state court to review and reverse, . . . depriving each court of its power" and possibly resulting in "conflict and confusion." *Id.* at 275.

The section-by-section analysis of Public Law 100-352, which revised § 1257, additionally makes clear that Lively's appeal is barred:

> Section 7 provides that this act shall become effective ninety days after enactment, but that the act shall not affect cases then pending in the Court or judgments or decrees *subject to appeal* that have been issued *prior* to the effective date of this act.

H.R. Rep. No. 660, 100th Congress, 2nd Sess. 12, *reprinted in* 1988 U.S. Code Cong. & Admin. News 766, 779 (emphasis supplied). The court of appeals judgment was not "subject to appeal" to this Court until state remedies had been exhausted.

In fact, the objective of the "highest state court" requirement of § 1257 is to insure that state remedies have been exhausted *before* resort to this Court may be had. *See, e.g., Costarelli v. Massachusetts,* 421 U.S. 193, 196 (1975).

Therefore, the amendment to § 1257 forecloses Lively's appeal.

III. Statement of the Case Relevant to Other Grounds for Dismissal

A. The Parties.

Valero is a public utility *intrastate* gas pipeline

company that purchases, transports, and sells natural gas throughout the State of Texas.

Lively is comprised of producers, operators, royalty interest owners, and sellers of oil and gas in Texas.

B. The Contract.

On February 12, 1973, Lively and Valero's predecessor-in-interest entered into a gas purchase contract ("Contract") for the sale of natural gas produced from Lively's properties in Sutton County, Texas. The Contract includes a "take-or-pay" provision:

> *Subject to the other provisions hereof,* Buyer agrees to purchase and pay for (or, *if Buyer's performance hereunder is not excused by other provisions of this agreement,* pay for, *if available,* whether taken or not) during the days of each Contract year . . . a *Daily Contract Quantity* of gas from Seller's Lands and Leases in the Contract Area equal to ninety percent (90%) of Seller's daily *Deliverability* of gas hereunder.

(Contract, art. V, § 5.3) (emphasis supplied).

The take-or-pay provision references two specific terms that are defined in the Contract and that operate with the take-or-pay clause to set forth Valero's take-or-pay obligations: "Daily Contract Quantity" ("DCQ") and "Deliverability." The Contract defines "DCQ" as "the quantity of gas per day, averaged over each contract year, which Buyer is required to take from Seller hereunder at the point of delivery specified in this Agreement." (Contract, art. I[e].)

Since the Contract states that the DCQ is 90% of *Deliverability*, the extent of any take-or-pay obligation must be measured in accordance with the specific Contract definition of "Deliverability":

> [T]hat quantity of gas which Seller *has available for delivery* from the Lands and Leases to Buyer during each day, in conformity with the requirements of this Agreement, at a constant rate of flow, when Seller's wells and facilities are not produced in excess of their maximum efficient rate of flow, but *not exceeding the maximum (including overproduction) rate of flow permitted by the laws, rules and regulations of the Railroad Commission of Texas or other governmental regulatory agency having jurisdiction*. Buyer agrees to make nominations, or to cooperate with Seller in the making of nominations, for well allowables (to be fixed or permitted by rules, regulations or orders of the Texas Railroad Commission) sufficient to cover the daily quantities which from time to time Buyer is entitled and elects to take hereunder up to the maximum quantity which in accordance with good engineering and gas production practice can be produced from Seller's wells in the field.

(Contract, art. I[j]) (emphasis supplied.)[1]

---

1. Although in its Jurisdictional Statement Lively references Contract language specifying how purely physical deliverability is to be tested and terms it the "specific use" of the term "deliverability" (Jurisdictional Statement, pp. 7-8), throughout trial the definition in art. I(j) was accepted as the proper definition of Deliverability by *both sides*. Lively submitted only the definition of Deliverability in art. I(j) as an instruction in its proposed charge.

Most of the Contract provisions cited herein are also set forth in the court of appeals opinion. (Lively's Appendix to Jurisdictional Statement, pp. 18-20).

Thus, the Contract's take-or-pay provision requires Valero to take, or pay for *if available*, 90% of the quantity of gas Lively has *available for delivery, not to exceed the maximum production allowed by the Railroad Commission of Texas* ("Commission").[2]

The take-or-pay provision was included to reassure Lively that Valero would not discriminate against Lively by taking gas from a producer with a lower price to the exclusion of Lively, whose gas in the subject area was dedicated to the Contract.

The Contract also includes what Lively calls a "governmental regulation" clause, expressly making the Contract *subject to* Texas laws and the rules and regulations of an "authority having jurisdiction" such as the Commission:

> This Agreement is made *subject to* all valid applicable federal and state laws or city ordinances, and to the orders, rules and regulations of any duly constituted federal or state regulatory body or authority having jurisdiction.

(Contract, art. XIII, § 13.1.)

Additionally, the parties included a *force majeure* clause, specifying "temporary failure of wells or sources of supply of gas, or market" as events of *force majeure*. (Contract, art. XII, §§ 12.1, 12.2).

C. Relevant Laws and Regulations.

The Texas Natural Resources Code ("Code") accords the Commission authority to regulate the drilling,

---

2. Valero and Lively agree that they are at all times subject to the regulatory authority of the Commission. Tex. Rev. Civ. Stat. arts. 6050-53 (Vernon 1962 and Vernon Supp. 1987); Tex. Nat. Res. Code Ann. Sec. 81.051, 111.081 (Vernon 1978).

production, transportation, and use of natural gas in Texas. The Code: defines "waste" as *"the production of natural gas in excess of* transportation or market facilities or *reasonable market demand* for the type of gas produced," Code § 86.012; declares "waste" to be unlawful, Code § 86.011; and charges the Commission with adopting "all necessary rules" to prevent it. *See generally* Code §§ 85.051, 85.052, 86.001, *et seq.*, 111.081, *et seq.* (Vernon 1978 and Vernon Supp. 1987).

The Commission also implements the Code's goal of "compelling *ratable* production," Code § 86.001, and carries out the Texas Common Purchaser Act's stipulation that a pipeline such as Valero must purchase gas without discrimination in favor of certain producers in a field and without unjust or unreasonable discrimination between fields in Texas. Code § 111.083 and § 111.086.

To discharge its Code-prescribed duties of conserving Texas' natural gas in an equitable manner, in 1978 the Commission adopted a system to "prorate" natural gas production — i.e., to determine the overall quantity of natural gas that should be produced in Texas in a given month and to assure that each producer is allowed to produce his fair share of that amount. The heart of this system is known as the Gas Market Demand Rule. 16 Tex. Admin. Code (§ 3.91) "§ 3.91" (prior to 9/1/86) and 16 Tex. Admin. Code § 3.30 ("§ 3.30") and § 3.34 ("§ 3.34") (from and after 9/1/86, as amended effective 3/2/87) ("Gas Market Demand Rule" or "Rule") (Lively's Appendix to Jurisdictional Statement ["Lively's Appendix"], pp. 286-303).

Valero and Lively agree on what the Rule requires. First, it requires an intrastate pipeline company such as

Valero: (i) to limit its purchases of gas from producers to proportionate shares of the pipeline's downstream market demand; (ii) to allocate its purchases "ratably" (without discrimination) among its various producers; and (iii) to purchase various categories of gas, established by the Commission, in a specified order of priority. (Lively's Appendix, pp. 288-92, 296-303).

Second, it proscribes a producer such as Lively from *producing* gas in excess of its ratable share of its purchaser's downstream market demand. (Lively's Appendix, pp. 286-87).

To ensure that production and takes are in accordance with market demand, the Rule explicitly sets forth steps that producers and pipelines must follow each month. Based on these specified procedures a pipeline then purchases gas from its sellers without discrimination and in accordance with the priority categories established by the Commission.

The overriding goal of Texas' regulatory scheme is to ensure that natural gas production does not exceed market demand and result in statutorily defined "waste," and that the market demand is fairly apportioned among producers.

D. The Interface Between the Gas Market Demand Rule and the Contract.

Pursuant to the *parties' own agreement* as reflected throughout the Contract, the take-or-pay provision and Gas Market Demand Rule work in tandem to define Valero's take-or-pay obligations. Both Valero's obligation to take and its alternative obligation to pay are limited *by the Contract's own terms* to the quantity Lively has

"available for delivery," "not exceeding the maximum rate of flow permitted by [Commission rules and regulations]." (Contract, art. V, § 5.3; art. I[j]). The Rule therefore governs the amount of gas Lively can have "available for delivery" at a given time, and establishes that the "maximum . . . rate of flow" under the Contract can never exceed Lively's ratable share of Valero's downstream market demand.[3]

It was undisputed at trial (and Lively has not argued otherwise in its Jurisdictional Statement or pleadings before the courts below) that *during the Contract years in issue Valero nominated, requested, took, and paid for Lively's ratable share of all gas for which Valero had a downstream market demand.*[4]

Any quantity exceeding the amount Valero actually took from Lively, therefore, could not be produced pursuant to Commission rules. The Contract *by its own terms* did not require Valero either to take or to pay for that amount of gas.

E. Lively's Lawsuit and Appeal.

Lively sued Valero for purportedly breaching the take-or-pay clause for the Contract years 1982-1985.

---

3. It is worth noting that the Gas Market Demand Rule also established procedures preventing the discrimination the take-or-pay clause was originally included to discourage.

4. The undisputed testimony at trial showed that a natural gas "market" is a function of price. The Commission requires Valero to charge an inflexible price for its gas equal to the weighted average of gas ("WACOG") plus $0.15. Over the past few years Valero's WACOG plus $0.15 has equalled $4.00 to $4.20 per MMBtu of natural gas. Therefore, Valero's sales market is the market for $4.00 gas. Prices for natural gas have fallen, and the evidence showed that that market, during the contract years in issue, was very small.

The trial court submitted the take-or-pay claims to the jury in Special Issue No. 2, which asked: "Do you find that Valero failed to take or pay for an amount of gas equal to the Daily Contract Quantity ("DCQ")?" (Lively's Appendix, p. 9). Special Issue No. 2 was accompanied by instructions setting forth the relevant Contract provisions and regulations. (*Id.*, pp. 10-12). The jury answered Special Issue No. 2 "no," and the trial court entered a take-nothing judgment against Lively on its take-or-pay claim. (Lively's Appendix, p. 2).

After unsuccessful appeals to the Texas appellate courts, Lively now attempts to invoke this Court's jurisdiction by presenting two questions upon which it predicated *no objection* in the trial court and which were not asserted in points of error until its *motion for rehearing* before the court of appeals:

1. Whether the Railroad Commission of Texas Gas Market Demand Rule as applied by a Texas Court of Appeals voiding take-or-pay obligations and liability in a natural gas purchase contract is preempted by the Natural Gas Policy Act.

2. Whether the Railroad Commission of Texas Gas Market Demand Rule as applied by a Texas Court of Appeals voiding take-or-pay obligations and liability in a natural gas purchase contract violates the Commerce Clause of the United States Constitution.

(Jurisdictional Statement, p. I).

Not only were these questions tardily raised, Lively's argument concerning them embodies a complete mischaracterization of Valero's position and the court of

appeals opinion. Lively has erroneously asserted that Valero relies on the Gas Market Demand Rule as *unilaterally abrogating* or "voiding" otherwise existing contractual obligations:

> Valero seeks to avoid its obligations under [the take-or-pay] provision by asserting that the Railroad Commission Gas Market Demand Rule *abrogates* the take-or-pay provision . . .

(Lively's Appendix, p. 85) (emphasis supplied.)

However, as Valero has consistently maintained, whether the Rule unilaterally *abrogates* the take-or-pay provision is *not the issue* in this case. Rather, the issue is simply the interpretation of *this* Contract, in which the *quantity* of gas Valero is required to take *or pay for* is *defined* as an amount "available for delivery," "not exceeding the maximum . . . rate of flow permitted by [Commission] rules." (Contract, art. I[j].) The Contract does not require Valero's *payment* for a minimum quantity of gas as measured in Mcfs or Btus; it requires payment for a certain percentage of "Deliverability," a defined term that embodies any limitations on production by Commission rules and regulations.

Lively's entire argument is therefore based on a faulty premise, and ignores the plain words of this Contract. In essence, through this appeal Lively seeks to *rewrite* the Contract to delete its provisions that Valero's payment obligations are limited to payment for gas that can be legally produced. The logical extension of Lively's position, moreover, is that no party can ever contract, in a take-or-pay provision, to limit its payment obligation to payment for gas that can be legally delivered.

Lively also mischaracterizes the court of appeals' holding:

> [T]he effect of the Texas Court of Appeals' reliance upon the governmental regulation clause is to hold that the Texas Gas Market Demand Rule relieves *all* pipeline purchasers in Texas of their take-or-pay obligations under *all* of their natural gas contracts in the absence of an express provision to the contrary.

(Jurisdictional Statement, p. 12) (emphasis supplied).

It bears noting that the court of appeals did not predicate its analysis simply on the "governmental regulation clause" (Contract, art. XIII, § 13.1; *see* page 9, supra). Rather, it cited other relevant provisions of the Contract as well, including and emphasizing the definition of Deliverability. (Lively's Appendix, pp. 3-4). Of even more significance, however, the court of appeals nowhere held that all pipeline purchasers are relieved of all their take-or-pay obligations. Rather, it held that under the terms of the Contract, and in light of the undisputed evidence that Valero nominated and requested all of Lively's gas for which it had a downstream market demand, Valero had no liability to Lively. The plain words of the Contract compel dismissal of this appeal.

IV. Lively Failed to Timely Raise the Points of Error Upon Which it Appeals to This Court.

This Court should dismiss this appeal because "the federal question sought to be reviewed was not timely or properly raised and was not expressly passed on. . . ." Sup. Ct. R. 16(b), 28 U.S.C.A. 30-31 (1984).

The issues Lively raises in this appeal were not expressly passed on by the courts below. Moreover, Lively acknowledges it did not raise these points of error until its motion for rehearing to the court of appeals (Jurisdictional Statement, p. 4), which was untimely as a matter of law. Valero complained of this untimeliness in its Response in Opposition to Appellant's Motion for Rehearing in the court of appeals (Valero's Appendix, pp. 94-95) and Reply to Application for Writ of Error (Valero's Appendix, pp. 143-44).

Tex. R. App. P. 52(a) states:

> In order to preserve a complaint for appellate review, a party must have presented to the trial court a timely request, objection or motion, stating the specific grounds for the ruling he desired the court to make if the specific grounds were not apparent from the context.

Additionally, a party must assign a point of error concerning the matter complained of in its *initial* brief to the court of appeals; a motion for rehearing is too late. *Watson v. Glens Falls Ins. Co.*, 505 S.W.2d 793, 797-98 (Tex. 1974); *Lone Star Gas Co. v. Sheaner*, 305 S.W.2d 150, 153 (Tex. 1957); *Gillen v. Diadrill, Inc.*, 624 S.W.2d 259, 264 (Tex. App.—Corpus Christi 1981, writ dism'd); *see* Tex. R. Civ. P. 74(d).

Lively claims its points of error were raised at the first opportunity because, it contends, the court of appeals opinion *created* the federal question.

This assertion is incorrect. Lively's contention that a federal question exists is predicated on its mistaken notion that the court of appeals applied the Gas Market

Demand Rule to unilaterally void Valero's take-or-pay obligations under the Contract, with such an application allegedly resulting in preemption.

This purported application was the same complaint upon which Lively based many of its other arguments before the court of appeals in its initial briefing. For example, Lively's points of error 1 and 2 before the court of appeals contended the trial court erred "in admitting evidence of the . . . Rule" and "in including the . . . Rule [as an] Instruction . . . to Special Issue 2," both errors arising "because, as a matter of law, the Texas gas market demand rule does not relieve Valero of its contractual obligation to pay for the Daily Contract Quantity of gas. . . ." (Valero's Appendix, pp. 3, 10). The court of appeals opinion similarly explained Lively's contention as that the Rule "did not relieve Valero of its contractual obligation." (Lively's Appendix, p. 5).

By arguing that the Rule did not in and of itself relieve Valero of its take and payment obligations "as a matter of law," Lively was essentially complaining that the Rule was applied at trial to unilaterally abrogate Valero's contract rights, the same "application" Lively contends would result in federal preemption and impinge on the Commerce Clause. Since the same fallacious reasoning underlying many of Lively's initial arguments before the court of appeals also underpins these points of error, they also could have been raised before the motion for rehearing.

In fact, purported "amici curiae" (who actually were interested parties litigating against Valero), in a brief submitted to the court of appeals before it ruled, raised these very issues: "An incorrect holding that the

Texas conservation and prorationing statutes and regulations interfere with take-or-pay obligations will result in preemption of those statutes and regulations by federal law." (Valero's Appendix, p. 148). Although the court of appeals denied the amici leave to file their brief, if the amici raised these arguments earlier, Lively could have.[5]

The cases Lively cited do not support its proposition. In *Herndon v. State of Ga.*, 295 U.S. 441 (1935), for example, this Court held that the federal question was *not* timely raised:

> The federal question was never properly presented to the state supreme court unless upon motion for rehearing; and that court then refused to consider it. The long-established general rule is that the attempt to raise a federal question after judgment, upon a petition for rehearing, comes too late, unless the court actually entertains the question and decides it.

Id. at 443. While noting an exception to the rule — "if the ruling of the state court could not have been anticipated" — the Court held that the exception was not present, because a similar ruling made in another case rendered the petitioner "bound to anticipate the probability of a similar ruling in his own case, and preserve his right to a review here by appropriate action, . . ." *Id.* at 445.

Here, Lively obviously could have anticipated what it contends was the ruling of the court of appeals — that

---

5. Points of error are only properly preserved for appeal if asserted in *appellant's* brief. *See, e.g., Samples Exterminators v. Samples*, 640 S.W.2d 873, 875 (Tex. 1982); *Frio Investments, Inc. v. 4IMC/Rohde*, 705 S.W.2d 784, 787 (Tex. App.—San Antonio 1986, writ ref'd n.r.e.); *Norton v. Martin*, 703 S.W.2d 267, 273 (Tex. App.—San Antonio 1986, writ ref'd n.r.e.).

the Gas Market Demand Rule voided contract rights — because it predicated other points of error before the court of appeals on the same basic complaint, and "amici" made the preemption argument *prior* to the court of appeals' ruling.

The other cases cited involved new points of error raised after a court's truly unpredictable reversal or reinterpretation of previously valid law. *Great N. Ry. Co. v. Sunburst Oil & Refining Co.*, 287 U.S. 358 (1932) (lower court overruled previously valid law for future but not previous transactions, and appellant complained on rehearing of dual standard's unconstitutionality); *Brinkerhoff-Faris Trust & Savings Co. v. Hill*, 281 U.S. 673 (1930) (state supreme court overruled previously valid authority); *State of Mo. v. Gehner*, 281 U.S. 313 (1930) (state supreme court construed statute in a manner completely differently from the lower court and the administrative body from whom appeal was originally taken). In this case, the court of appeals did not overrule previously valid law, and to the extent Lively contends it did, Lively anticipated such a ruling in other arguments advanced prior to the court of appeals' ruling.

In *Clark v. Jeter*, 486 U.S. 456, 108 S. Ct. 1910 (1988), the petitioner argued that a Pennsylvania statute conflicted with a federal statute. In determining not to reach this preemption argument, this Court stated:

> Having reviewed the record, we find that Clark did not adequately present a federal pre-emption argument to the lower courts. It is our practice, when reviewing decisions by state courts, not to decide federal claims that were not "pressed or passed upon" below.

Id. at 1913. Lively did not timely press its preemption argument in the lower courts, and it is foreclosed.

Finally, Lively's failure to comply with Texas procedure by untimely asserting its points of error renders the court of appeals judgment sustainable on an adequate non-federal basis. *See* Sup. Ct. R. 16(b), 28 U.S.C.A. 30-31 (1984).

V. Lively Raises No Federal Question at All, Much Less a Substantial One.

Lively's Jurisdictional Statement raises no federal question. Lively does *not* claim that the Gas Market Demand Rule *per se*, as applied to intrastate pipelines, is preempted or impinges upon the Commerce Clause. Rather, Lively claims that the Rule suffers these infirmities only "as [it was] construed and applied by the court of appeals" in this case. (Jurisdictional Statement, p. 12). Indeed, Lively embraces the rulings of "other courts," reviewing different contracts, that it alleges "have recognized that contractual obligations to pay for gas not taken are not *superseded* by the Texas Gas Market Demand Rule." (Jurisdictional Statement, p. 18) (emphasis supplied).

As shown, however, Lively flatly misstates how the appellate court "construed and applied" the Rule. A plain reading of the court of appeals opinion discloses that it nowhere held Valero's or other pipelines' take-or-pay obligations were unilaterally *superseded* or "voided" by the Gas Market Demand Rule. Rather, the court of appeals found that Valero and Lively had *agreed* that the payment obligation was limited to legal deliverability. (Lively's Appendix, p. 4).

Recognizing that the take-or-pay clause itself and other Contract provisions it references entirely undermine its premise, Lively disingenuously implies in its Jurisdictional Statement that the court of appeals only relied on the "governmental regulation" clause. Lively contends, citing no authority whatsoever, that this provision is common in take-or-pay contracts, and that allowing it alone to implicate the Gas Market Demand Rule would render all take-or-pay provisions ineffective. Whether this unsubstantiated assertion is true or not, and without analyzing the effect of the "governmental regulation" clause standing alone, the court of appeals opinion in fact referenced and emphasized other relevant Contract provisions. (Lively's Appendix, p. 4). The take-or-pay provision itself, read in conjunction with the definitions of DCQ and Deliverability, limits Valero's take *and* payment obligations to an amount Lively could legally produce and Valero could legally take. Nowhere in its Jurisdictional Statement does Lively suggest *any* error would have resulted from the court of appeals' reliance on those provisions, tacitly conceding such reliance rendered the opinion proper. Therefore, even accepting *arguendo* Lively's assertions and analysis, state law contract interpretation controls, and no federal question is presented. At the very least, independent state law grounds (the other Contract provisions interpreted in accordance with state law) support the court of appeals' judgment.

Moreover, no federal question would be presented even were Lively's interpretation of the court of appeals opinion correct. The cases Lively cites, *Northern Natural Gas Co. v. State Corp. Comm'n of Kan.*, 372 U.S. 84 (1962), *Transcontinental Gas Pipeline Corp. v. State Oil & Gas Bd. of Miss.*, 474 U.S. 409 (1986) ("*Transco*"),

and *ANR Pipeline Co. v. Corporation Comm'n of the State of Okla.*, 860 F.2d 1571 (10th Cir. 1989), *cert. denied*, ____U.S.____, 109 S. Ct. 1967, 104 L.Ed.2d 435 (1989), all involved the application of state regulations to *interstate* pipelines, and actually underscore the *absence* of a rationale for preemption here.

In *Transco*, for example, in holding a ratable take order preempted for interstate pipelines, this Court noted in part that Transco's compliance with Mississippi's law "disturbs the uniformity of the federal scheme, since interstate pipelines would be forced to comply with varied state regulations of their purchasing practices." 474 U.S. at 423. Similarly, this Court in *Northern Natural Gas Co.* struck down the state orders at issue because they affected the ability of the Federal Power Commission, in part, to "achieve the uniformity of regulation which was an objective of the Natural Gas Act." 372 U.S. at 91-92. As an *intrastate* pipeline Valero is not subjected to "varied" practices.

The second rationale for preemption advanced in *Transco* — that the ratable take order would increase the ultimate price to consumers by forcing a pipeline to take noncontract gas in favor of contract gas, incurring take-or-pay liability — does not support, and in fact undermines, Lively's position. *See Transco*, 474 U.S. at 423. Valero's price would not be affected by the Rule under the *Transco* rationale. Accepting solely *arguendo* Lively's assertion that the Rule "as construed and applied" by the court of appeals "voids" take-or-pay obligations, any resulting effect on interstate commerce, by the *Transco* analysis, could only be a beneficial one. As this Court in *Transco* implicitly recognized, such an avoidance could only *reduce* prices borne by consumers, since pipelines

that must pay for gas they cannot take, and that are allowed to increase their prices, pass through such take-or-pay payments to consumers.

Finally, the Gas Market Demand Rule is fundamentally a regulation of production, since it precludes a producer from producing in excess of its ratable share of a purchaser's downstream market demand. (Lively's Appendix, pp. 286-87). Production regulation is not preempted by federal law even as it affects interstate pipelines. *Northwest Central Pipeline Corp. v. State Corporation Comm'n of Kan.*, ___U.S.___, 109 S. Ct. 1262, 1274-75, L.Ed.2d 509 (1989).

The Rule similarly does not impinge upon the Commerce Clause. In *Pike v. Bruce Church, Inc.*, 397 U.S. 137 (1970), this Court noted that a statute or regulation should be upheld where the statute regulates evenhandedly to effectuate a legitimate local public interest, and its effects on interstate commerce are only incidental, unless the burden imposed on interstate commerce "is clearly excessive in relation to the putative local benefits." 397 U.S. at 142. Protecting correlative rights is a legitimate state interest. *Northwest Central Pipeline Corp.*, 109 S. Ct. at 1278. As shown, the Rule as Lively claims the court of appeals construed it can have no significant impact on interstate commerce, and clearly cannot impinge on the Commerce Clause under the *Pike* test.

Lively cites no authority suggesting that state regulatory schemes applying to intrastate pipelines are preempted or encroach upon the Commerce Clause. In fact, this Court has distinguished between intrastate and interstate pipelines when considering such questions. *See Exxon Corp. v. Eagerton*, 462 U.S. 176, 185-87 (1983).

Lively presents no federal question, and its appeal should be dismissed.

VI. The Judgment of the Court Below Should be Affirmed.

The judgment of the court of appeals is plainly correct and should be affirmed. The Contract limits Valero's take and payment obligations to the amount of gas that can be legally produced, which the Gas Market Demand Rule specifies to be Lively's ratable share of Valero's downstream market demand. It is undisputed that Valero took and paid for the amount of gas Lively could legally produce. Therefore, the court of appeals' judgment was correct and should be affirmed.

VII. Conclusion and Prayer

In conclusion, Valero respectfully prays: that Lively's appeal be dismissed; alternatively, that the judgment of the court of appeals be affirmed in all respects; and that Valero be awarded its costs in this appeal.

Respectfully submitted,

J. Clifford Gunter III

J. CLIFFORD GUNTER III

BRACEWELL & PATTERSON
2900 South Tower Pennzoil Place
Houston, Texas 77002
(713) 223-2900

Counsel for Valero Transmission Company, Appellee

CERTIFICATE OF SERVICE

I hereby certify that three true and correct copies of this Motion to Dismiss Appeal, and, Alternatively, to Affirm Judgment have been served on appellant by depositing an envelope containing them in a United States post office or mailbox, with first class postage prepaid, on January 8, 1990, addressed to Jesse P. Luton, Jr., Scott, Douglass & Luton, 4300 NCNB Center, 700 Louisiana Street, Houston, Texas.

J. Clifford Gunter III

J. CLIFFORD GUNTER III